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Protected Equity Frame



Systematic Multi-Asset Strategy with Black Swan Protection



DEECKE FINANCIAL SOLUTIONS
Private Wealth Experts



STRATEGY KEY INFORMATION

Investments are always associated with risks. And risks are also opportunities. We believe in making the most efficient and diversified use of opportunities in the form of various management strategies.

We do not speculate on economic data and market prospects, because nobody can predict the future!

After 30 years of experience in the capital market, we know that there is no single system that always works!

That is why DEECKE Financial Solutions use several systems at the same time, which either substitute or complement each other depending on the market situation.

The “Protected Equity Frame Strategy” portfolio is aimed at institutional and private investors, who are qualified to invest in appropriate investments, and are looking for long-term capital growth with low volatility, a high Sharpe ratio and monthly liquidity.

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STRATEGY – COMPONENTS

1. L/S Equity with contrarian styles

on with the aim of providing stability

2. Options Combinations

one of four technical models with 5 different sources of return

3. Hedge

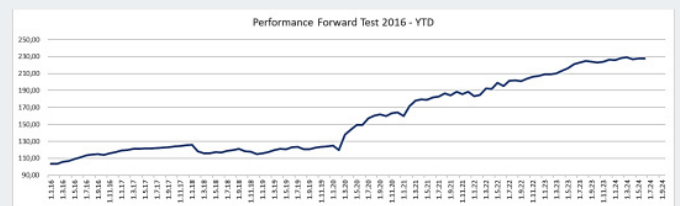
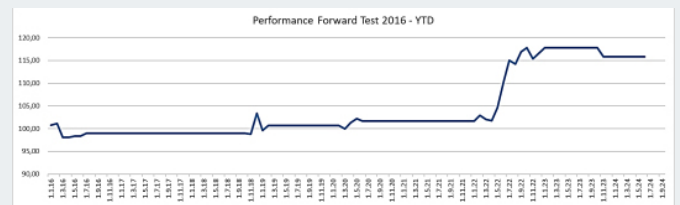
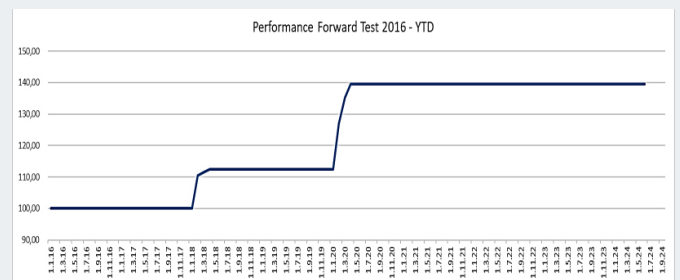
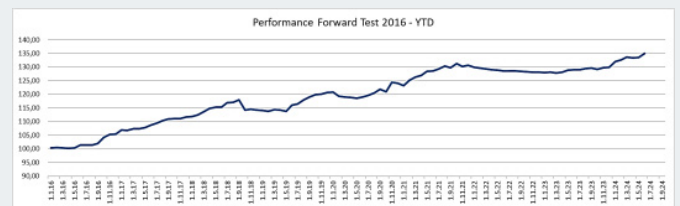
provides protection against “fat-tail” risks

4. Short Futures on Indices

In “bear markets” when bear-market strategies do not work, the short futures trades can compensate

5. VIX Futures

are the fourth source of alpha, substituting and complementing to the other three



INVESTMENT STRATEGY

The “Protected Equity Frame Strategy” is a multi-asset portfolio with 4+1 alpha-sources from overlay trading systems and a protection against strong downward movements.

The aim is to avoid high volatility in the portfolio and to always protect the invested capital while achieving high average returns.

The portfolio consists of several carefully selected investment strategies with as many contrarian styles as possible. The selected strategies have been set up since 2012 and have been exposed to a very rigorous analysis, applying a set of parameterized rules and criteria in terms of correlations, maximum volatility, value-at-risk and some other quality characteristics. The allocation within the portfolio is equally distributed according to the value at risk.

To reduce volatility, we apply four signal-driven overlay models that take advantage of various options and futures trading strategies and generate additional alpha, even in bear markets. A hedge position protects the portfolio from sharp price falls.

The result is a portfolio of different strategies and technical models that leads to a stable performance with a Sharpe ratio of around 2.0.

SHARPE RATIO

2.0

SETUP SINCE

2012

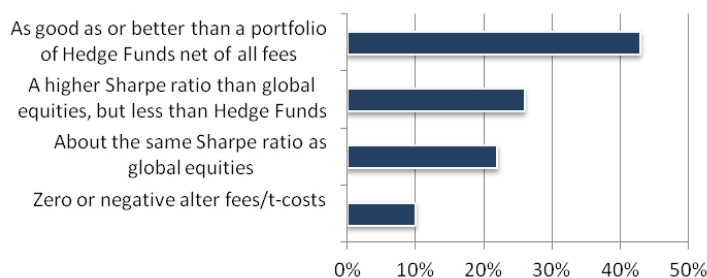


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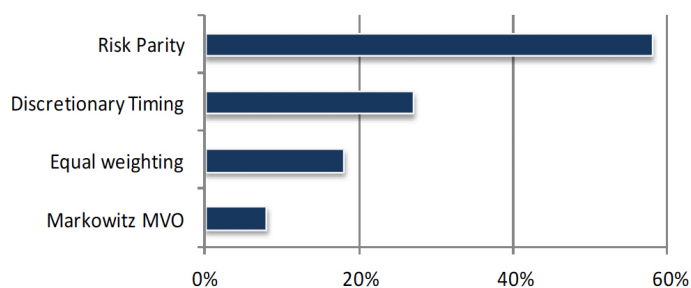
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THE MARKET TRENDS BY INVESTORS SURVEY RESULTS

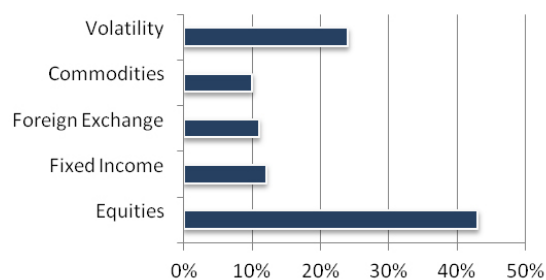
What are the long-term performance expectations for diversified risk factor portfolios?



Which risk-management approach will be the optimal over the next 3 years?



Which asset class will offer the best opportunity for Risk-Premium investing over the next 1 – 3 years?



Source JP Morgan Conferences 2014/2015

Volatility return depends on the average correlations, average volatility and cross-sectional dispersion in volatilities. Dispersion discount depends on cross-sectional dispersion in the underlying asset's growth rates and length of the evaluation period.

THE CONCLUSION OF THE TRENDS IN THE MARKET

Having analyzed the market trends we conclude that today's investors face an investment paradox.

THE CHALLENGES ARE

Sustainable low return

Debt
Demography
Deflation

OUR SOLUTIONS

Focus on positive returns

Combination contrarian styles
Variation of anti-cyclical strategies
Independent of economic cycles

Low risk budgets

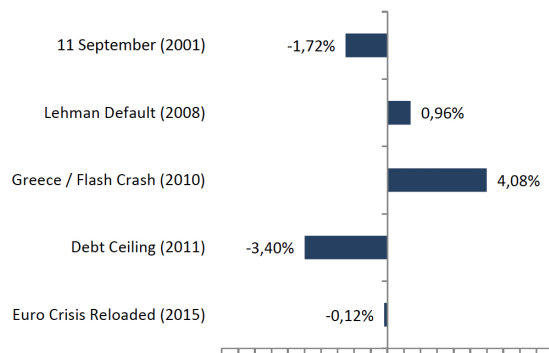
Intelligent risk budgeting
Sourcing of new risk budgets
Attractive return/risk profiles

Focus on return/risk-management

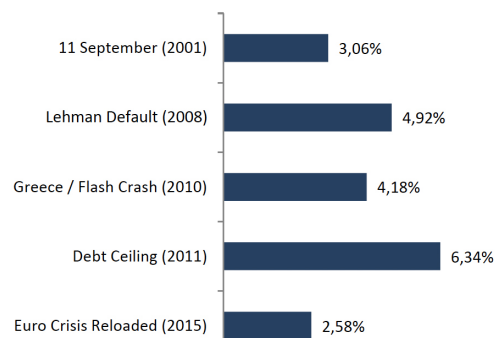
Identification & analysis of volatilities
Uncorrelated trading-models selection
Sharpe-ratio enhancing allocation

STRESS TEST OF THE PROTECTED EQUITY FRAME STRATEGY IN DIFFERENT SCENARIOS VS. BENCHMARK

Expected Changes



Expected Volatilities



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1. EQUITY STRATEGY: LONG – SHORT

The equity-classes and applied trading-models are subject to several selection criteria. This takes place via a programmed algorithm on a systematic and mechanical basis. Finally, the underlying models are allocated automatically based on the defined criteria.

The long-short equity strategy goal is to find empirically proven inefficiencies in the market, and to generate Alpha by using the opportunities of anomalies and certain enhancing effects such as:

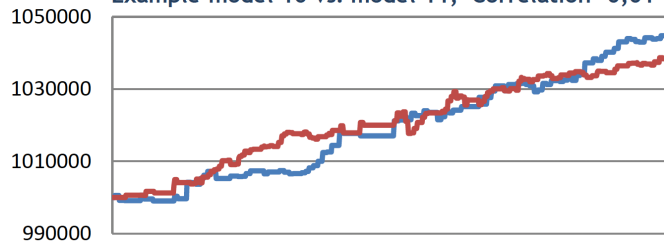
MOMENTUM EFFECT

MEAN REVERSION EFFECT

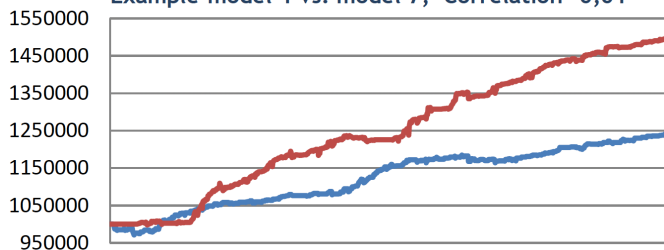
SEASONALITY EFFECT

Those effects mentioned above are some of the main drivers of our trading models that have proven to work as amplifiers to the performance of the portfolio.
In combination they helped to stabilize the volatility and enhance the Sharpe-ratio, thus confirming only positive annual returns so far.

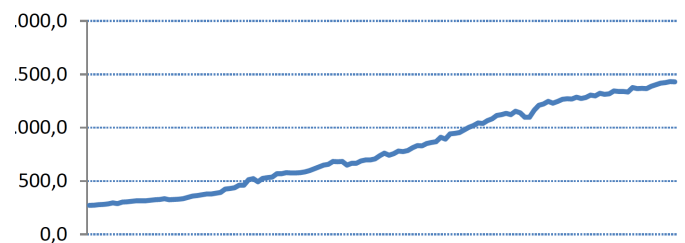
Example model 10 vs. model 11, Correlation -0,01



Example model 1 vs. model 7, Correlation -0,01



The result is, as shown in the graph below right, a well diversified and equated portfolio of many models with different styles and strategies that lead to an allocation with a sustainable return at a low average volatility and at a comparatively high yield, expressed in an attractive Sharpe-ratio between 1.7 and 2.3 .



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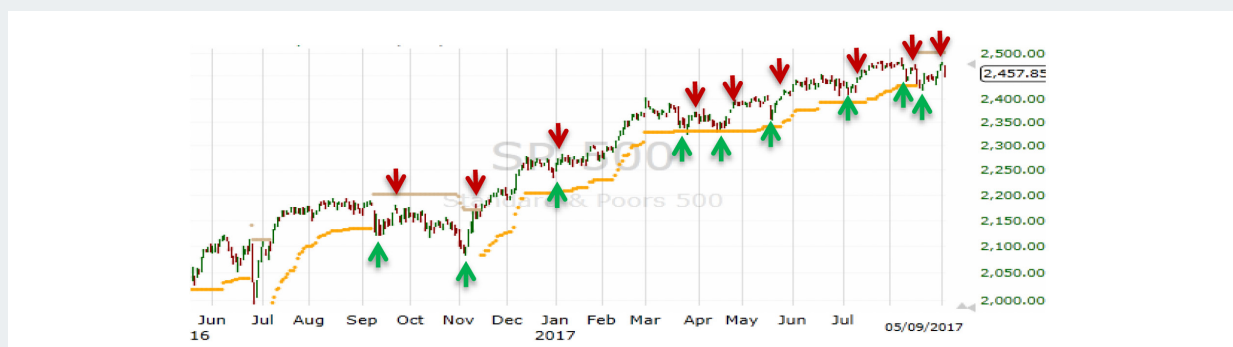
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1. EQUITY STRATEGY: LONG – SHORT

MEAN REVERSION EFFECT

Protected Equity Frame focuses on mechanical systematic and quantitative models. The long-short equity strategy purely aims at a systematic and mechanical quantitative investment approach. The quan-

titative approach ensures consistent and replicable trading-decisions. The systematic and mechanical execution stands for the independence of emotionally driven decisions and the avoidance of human trans-



mission mistakes.

Our strategy does not rely on any fundamental analysis. The fair value is exclusively generated by applying technical methods, mainly driven by the “mean reversion effect”.

The principal of the mean reversion resembles the classic value approach which can easily be described as:

**BUY AT THE LOWEST POSSIBLE
AND SELL AT THE
HIGHEST POSSIBLE PRICE!**



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1. EQUITY STRATEGY: LONG – SHORT

CORRELATION CHART

	1	2	3	4	5	6	7	8	9	10	11
1	1										
2	-0,3	1									
3	-0,85	0,36	1								
4	0,4	0,06	-0,29	1							
5	-0,51	0,02	0,59	-0,54	1						
6	0,04	0,24	0,06	0,71	-0,32	1					
7	-0,48	0,61	0,44	0,35	0,04	0,7	1				
8	-0,82	0,27	0,78	-0,41	0,73	0,01	0,5	1			
9	-0,01	-0,42	-0,09	-0,07	-0,15	-0,23	-0,39	-0,15	1		
10	0,42	0,05	-0,24	0,43	-0,54	0,31	-0,03	-0,42	-0,03	1	
11	-0,26	-0,11	0,26	-0,74	0,56	-0,8	-0,5	0,31	0,33	-0,31	1

The correlation-chart shows that not all the models necessarily need to be completely uncorrelated.

The key is the algorithmically applied combination of anti-cyclical strategies and contrarian styles, by also considering low and negative correlations to each other within different time frames. By doing so, positive returns of one model can equate negative results of another model and vice versa with a high probability during different periods of time. That reduces the portfolio's volatility and the risk of negative total returns and raises the Sharpe-ratio.

11 MODELS

Model 1	European Equities	Mean Reversion	Long Only
Model 2	US Equities Mean	Reversion	Long Only
Model 3	European Equities	Momentum	Long Only
Model 4	US Equities	Momentum	Long Only
Model 5	European Equities	Mean Reversion & Momentum	Long Only
Model 6	US Equities	Mean Reversion & Momentum	Long Only
Model 7	Indexfutures S&P500	Mean Reversion	
Model 8	IF S&P500, Nasdaq, Russel	Mean Reversion	
Model 9	Indexfutures S&P500	Volatility	
Model 10	Indexfutures S&P500	Seasonality	
Model 11	Indexfutures S&P500	Seasonality, Momentum	

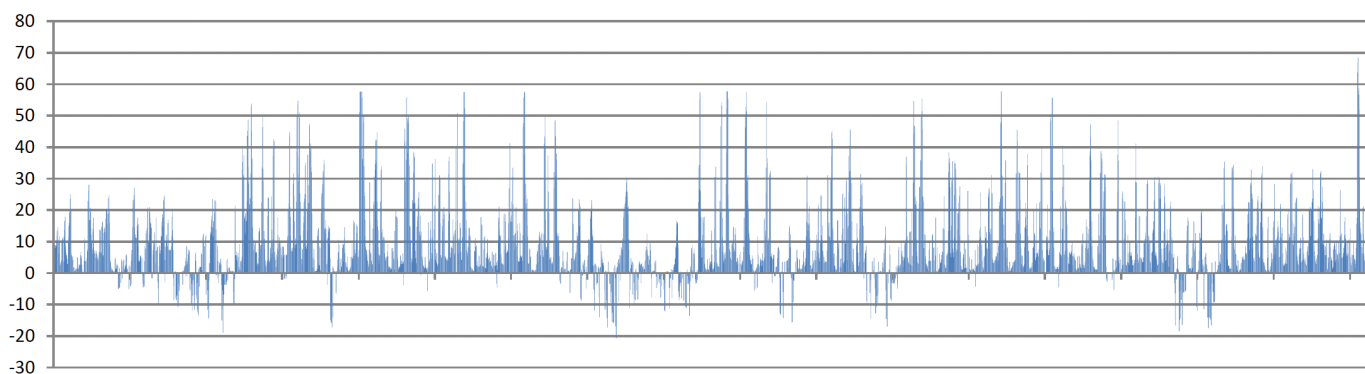
In all the 11 models trading signals are generated independently. None of the models is related to any other. The individual models are screened according to their maximum drawdown, Sharpe-ratio and their exposure during different market-stages. Next the algorithm quantitatively analyzes the criteria and defines the allocation of the individual models to the portfolio.

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1. EQUITY STRATEGY: LONG – SHORT

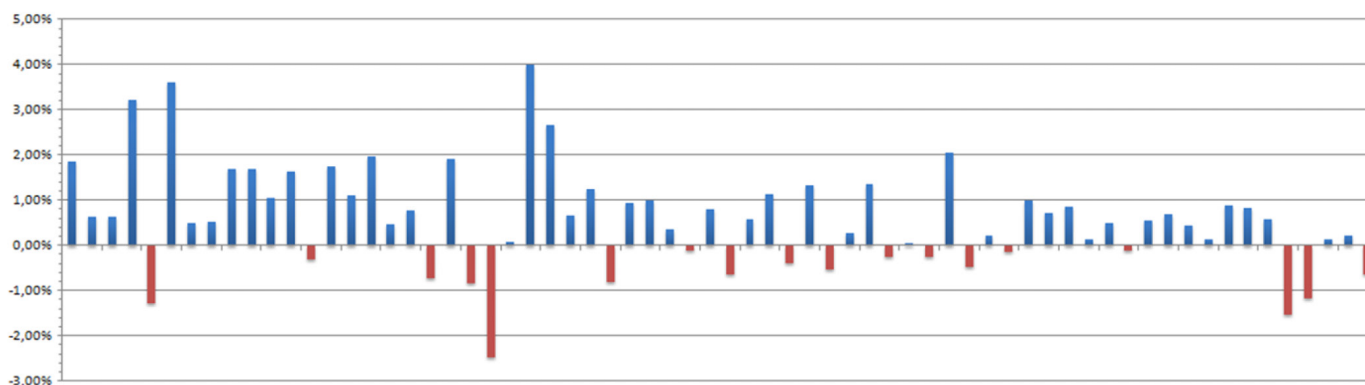
ALGORITHM



The algorithm automatically sets long exposures in up-trends and short exposures in down-trends. Positions are readjusted to the primary trend very fast. The portfolio does not maintain risky positions very long and rebalances its peak positions in a very

short period. Risky positions generally are kept within limits. The portfolio generally holds a long exposure according to the long bias of the stock markets. This method ensures limited risk and drawdown through fast recovery periods.

MONTHS



The long-short equity strategy achieved 73% positive months versus 27% negative months. The Strategy proves to be a portfolio with a moderate volatility of

below 4.0%. The maximum drawdown was 3.31%, the best month delivered 3.99%.

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THE ADDITIONAL ALPHA WITH THE OVERLAY STRATEGIES

2. Options

one of three technical models with 5 different sources of return

3. Hedge

provides protection against “fat-tail” risks

4. Short Futures on Indices

In “bear markets” when option strategies do not work, the short futures trades are used

5. VIX Futures

are the third source of alpha, substituting and complementing to the other two



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2. OPTIONS – SOURCES OF ALPHA

Forecast-free return sources are complemented by optimized entry points based on:

ALPHA SOURCE 1:

Overvaluation of options

ALPHA SOURCE 2:

Volatility arbitrage

ALPHA SOURCE 3:

Positive kurtosis

ALPHA SOURCE 4:

Use of a trend following model for strategic trend determination

ALPHA SOURCE 5:

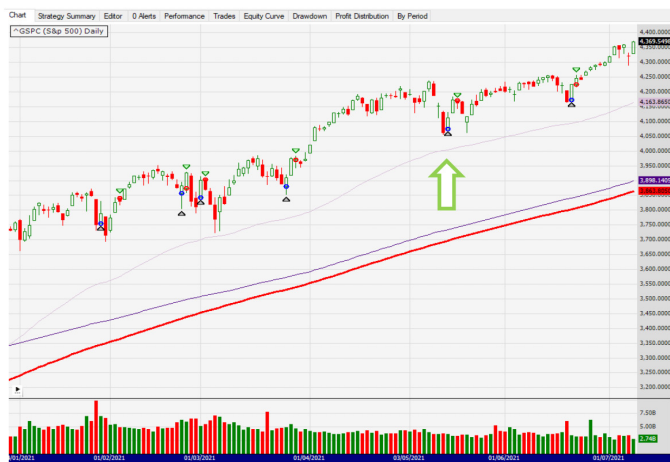
Use of a mean-reversion model for a tactical and more favorable market entry and optimization of premium Return through higher volatility in the VIX.

The only possible risk of loss with this complex option combination lies in a very sharp price decline directly after the entry or setup of the option strategy.

With the help of an optimization of the entry points by long-time proven systematic, quantitative trading models, the hit rate can be increased significantly, and volatility and loss risks can be reduced.

Both the trend-following model and the mean-reversion model are proven trading systems that have been used independently in equity trading for years. The option strategy combines a variety of highly differential alpha sources and consists of a “best-of” of success full trading systems, which have been further developed over the last 15 years based on our own trading successes and additionally on new scientific findings and research.

2. OPTIONS – EXAMPLE OF TRADES WITH OPTIONS



Every evening our quantitative algorithm generates screens of the market. When opportunities are found, we get the signals to build the options strategy.

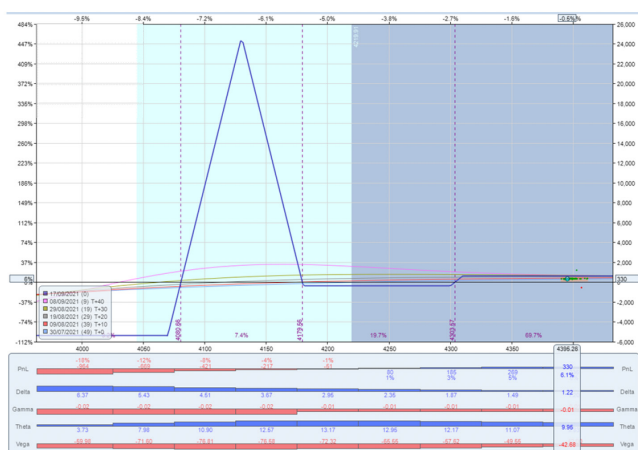
In the first step, the main market-trend is measured by a trend-following model.

In the second step, a separate mean reversion model provides us with specific entry signals.

The goal is an optimized positioning of option contracts with a high probability to resume the original uptrend.

2. OPTIONS – EXAMPLE OF TRADES WITH OPTIONS

EXAMPLE: SETTING S&P 500 OPTION-POSITION AT LEVEL 4175 BASED ON A PORTFOLIO-SIZE OF 100.000 EUR



The profit and loss of the option strategy varies in time until expiry date (blue line).

In fact, profit can be generated within a broad range of the price. As a practical example for that fact, we visualize in the chart on the left, that within the approximate term of 20 days remaining, the loss range would not start before the level of 4070 and 4080 points. For protection against strong sell-offs, a so-called “Black Swan Hedge” is positioned in the portfolio. This consists of long puts (Out of the money) and can be implemented almost cost-neutrally as of day 100.

3. RISK-MANAGEMENT AND HEDGE

1. General Risk-Management Methods

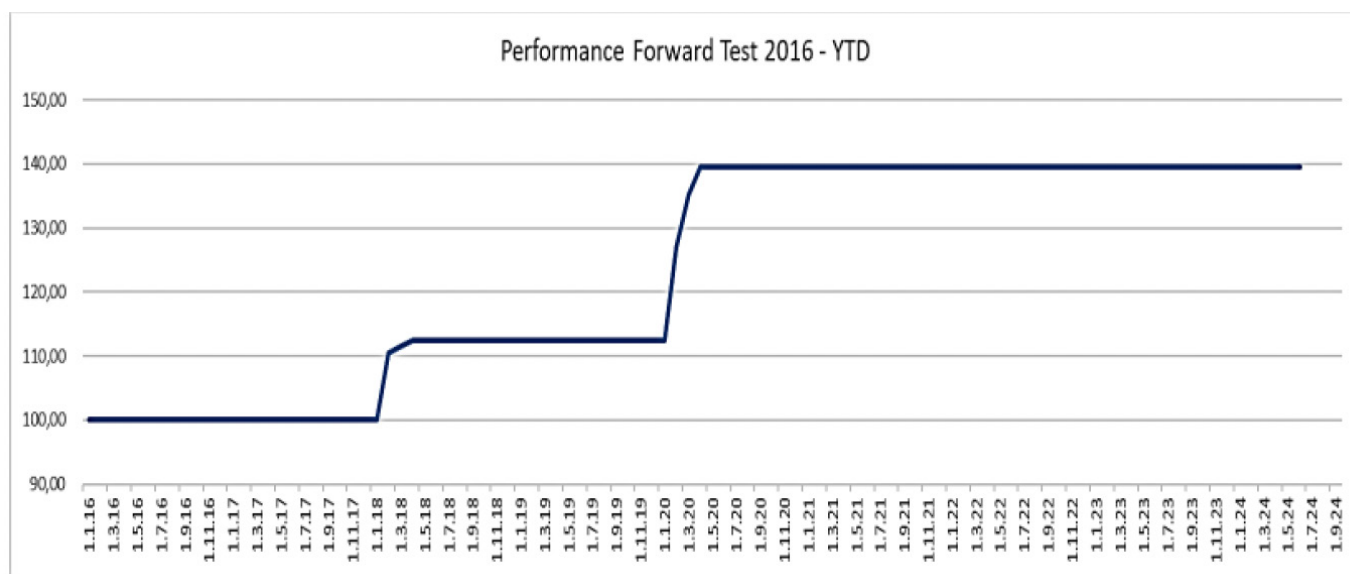
Only listed, liquid stock index options are used. This excludes single value risk. The portfolio is checked for possible risks by means of daily Value-at-Risk and stress test analyses. Real-time monitoring is used to monitor the portfolio positions and value floors for any necessary "follow-up" actions.

2. Options Combinations

Our complex option strategy does not contain any open short positions in its entirety. Each short option is covered by a corresponding long option and unlimited risks of loss are thus not permitted. The return and risk profile over the strategy period is clearly determined in advance.

3. Additional Protection of „Fat-Tail“ Risks

The sources of return are supplemented by an innovative hedging concept which can be setup "cost-neutrally" and which protects the option strategy in the event of an extreme increase in volatility and as strong sell-off. This hedging concept unfolds its effect in so-called „Black Swan Events". As a rule, in the case of regular market movements, our risk management is applied in a sustained and disciplined mechanical manner.



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4. SHORT FUTURES

The risk/reward ratio of the trade can thus be optimized, as the position is built up at more favorable (higher) prices. Losses in the event of a false signal can therefore be greatly reduced and at the same time the profit factor for positive trades can be significantly increased. Historically, this trading approach has a high hit rate of 72%.

Due to the high robustness of the futures overlay system, it is universally transferable to different indices. Our model currently uses the futures of the S&P500 and Nasdaq indices for implementation. High trading liquidity is always guaranteed here. DAX futures could also be used in the future.



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5. VIX FUTURES

With “Short VIX-Trading” we bet on a decline in the volatility index (VIX). The VIX measures the expected volatility of the S&P 500 share index over the next 30 days, based on the prices of S&P 500 options.

In short VIX trading, we are betting that market volatility will fall.

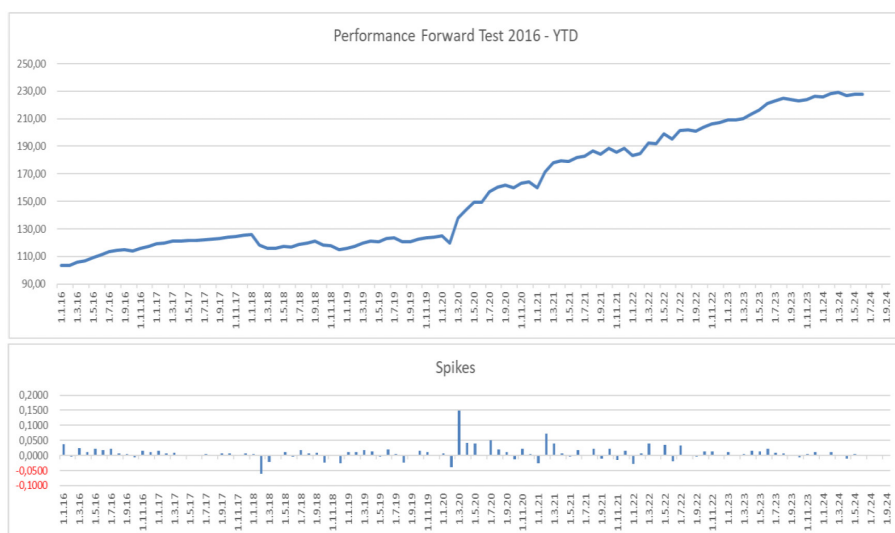
We focus on “short selling” VIX futures:

We sell futures contracts on the VIX in the expectation that their price will fall.

We use short VIX futures to speculate on a decline. We use classic, well-known and proven trading systems with various signals to build up positions:

Four different “mean-reversion” systems that differ from the length of the time measurement and the indicators we define Contango of the VIX futures against the VIX index and the steepness of the VIX futures curve

In addition, the ratio of the historical volatility of the S&P 500 to the VIX is measured and evaluated.



All signaling models are evaluated in the evening shortly before the official close of trading on the S&P 500.

If a minimum number of signals defined by us are positive, the positions are built up accordingly.

A cash position of approx. 10% of our current portfolio is deposited as a margin for this system.

SUMMARY

PROTECTED EQUITY FRAME STRATEGY



**NO
CREDIT RISK**



**LOW
VOLATILITY**



**HIGH
SHARPE RATIO**



**HIGH
STABILITY**

The Protected Equity Frame Strategy is a portfolio of several carefully selected systems with as many contrarian styles as possible with additional alpha from three signal-driven overlay models that take advantage of various options and futures trading strategies.

Different trading systems are combined to minimize volatility and drawdown, unlike competitors.

The sustainable and disciplined risk management and additional hedging also shield the portfolio from “black swan events”

As there is no system in the world, that will always work flawlessly, we use several systems simultaneously, which either substitute or complement each other depending on the market situation.



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ANNEX 2 – OPTIONS

The Alpha Sources of the Options Combinations



OPTIONS OVERLAY – SOURCES OF ALPHA

Our originality comes from the combination of three forecast-free models and two quantitative models:

ALPHA SOURCE 1:

Overvaluation of options

ALPHA SOURCE 2:

Volatility arbitrage

ALPHA SOURCE 3:

Positive kurtosis

ALPHA SOURCE 4:

Use of a trend following model for strategic trend determination

ALPHA SOURCE 5:

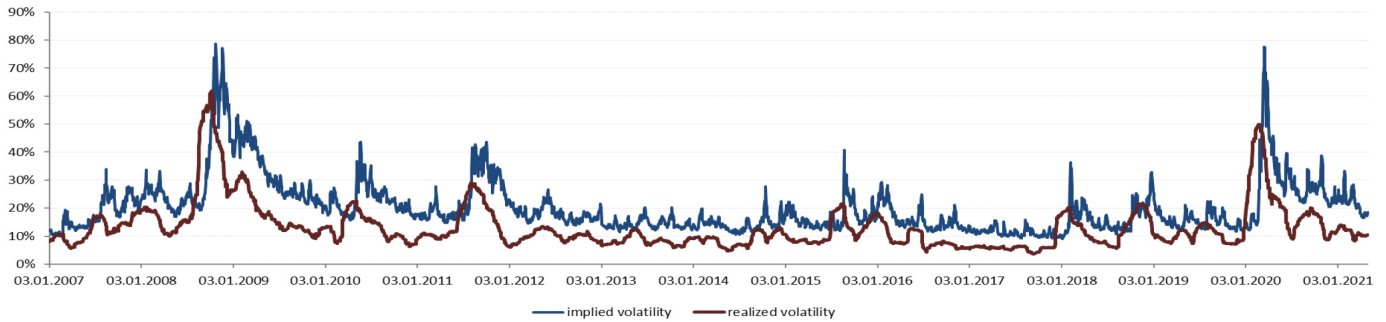
Use of a mean reversion model for a tactical and cheaper market entry and optimization of premium Return through higher volatility in the VIX

Forecast-free revenue sources are supplemented by optimized entry points based on:

With the help of an optimization of the entry points through systematic, quantitative trading models proven over many years, the hit rate can be significantly increased, and volatility and loss risks can be reduced.

SOURCE OF ALPHA NO. 1

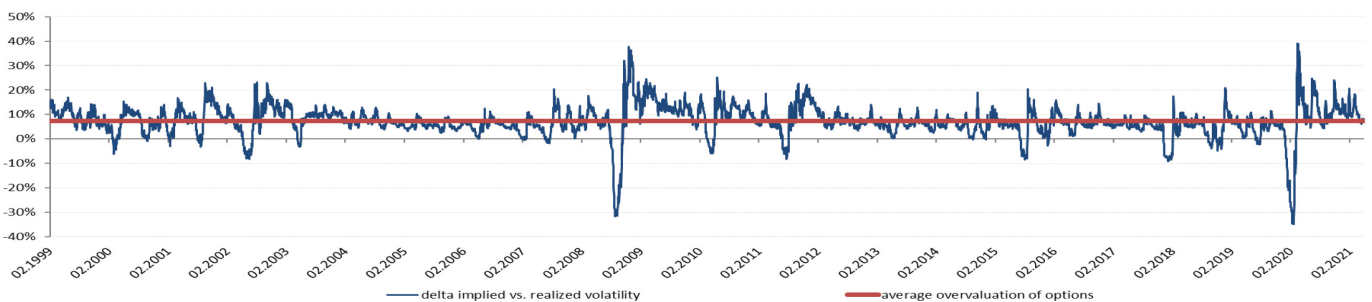
Example: overvaluation of options = implied volatility > realized volatility



Empirical studies show that implied volatility is significantly higher than historical or realized volatility in the long term. Implied volatility is derived from current option prices and can be understood as the measure of the range of fluctuation currently expected

on the market. Historical or realized volatility, on the other hand, is the actual range of fluctuation in the markets. Since implied volatility is now usually higher than realized volatility, an attractive risk premium can be collected here.

Example: overvaluation of options = implied volatility > realized volatility



For example, in the case of put options on the S&P500, the volatility premium is very pronounced. This can be collected by selling put options (option writer transactions) while maintaining high market liquidity.

Market participants are predominantly risk-averse. In anticipation of a market slump and high price fluctuations, they are prepared to pay a price for hedging their portfolio that is higher than a fundamentally

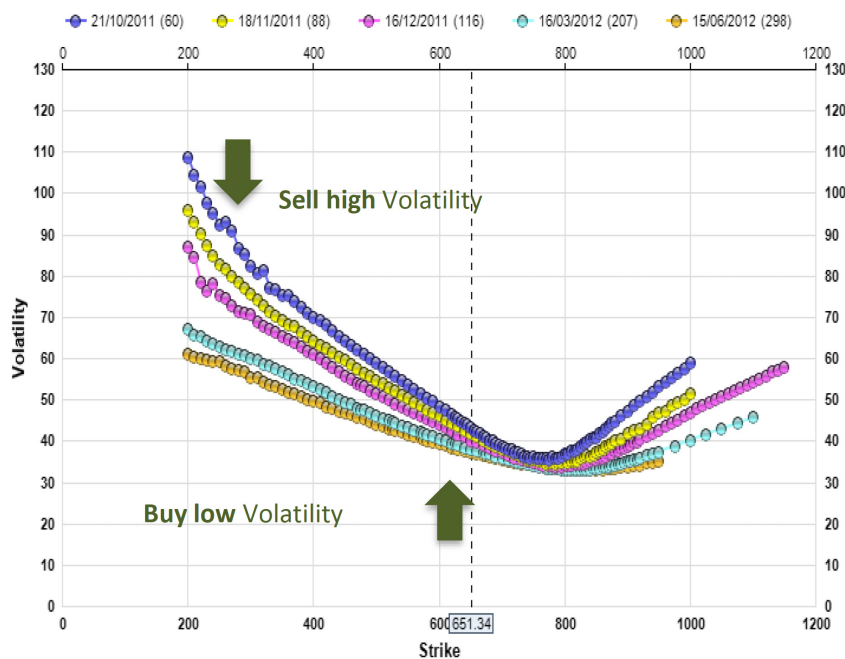
justified fair value. This creates a discrepancy between the expected and the actual risk and thus a delta as a usable volatility premium.

SOURCE OF ALPHA NO. 2

USE OF DIFFERENT OPTION VOLATILITIES, “VOLATILITY ARBITRAGE”

Implied volatility of different options on the same underlying are not necessarily the same. The “volatility smile/skew” describes the different volatility premiums for the same maturity, identical underlying but different strikes. A pronounced “volatility skew” can be found on the stock markets. Particularly, out-of-the-money put options are valued with a higher implied volatility than at-the-money put

options. There as on for this is that these are particularly suitable for hedging purposes as a favorable hedge against crashes and thus there is a higher demand for these put options. In addition, the historical return distribution on the stock markets shows a developed “left tail”. This means that large price losses occur more frequently than would be expected on the basis of the normal distribution.



The resulting volatility premium can be used to advantage in an options strategy. The algorithms in our strategy use this systemically existing imbalance of volatilities to design high-yield put strategies with low premiums and low risks:

WE BUY “CHEAP” VOLATILITY AND SELL “EXPENSIVE” VOLATILITY AT THE SAME TIME.

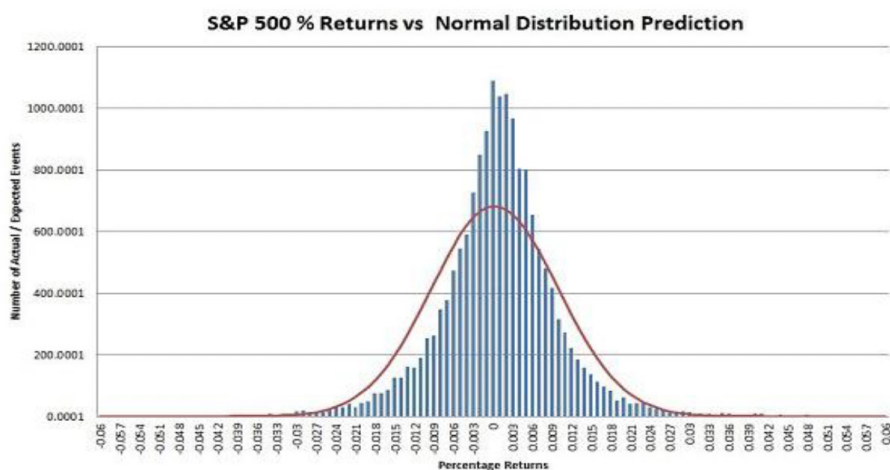
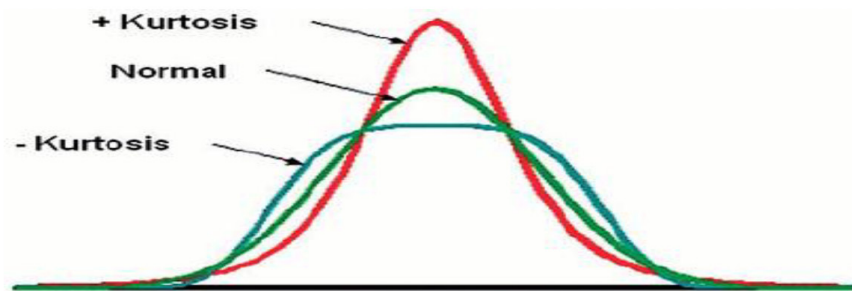
SOURCE OF ALPHA NO. 3

POSITIVE KURTOSIS (CURVATURE) OF THE YIELD DISTRIBUTION

The daily returns on the stock markets show strong deviations at the edges of the distribution curve on the one hand and a high positive curvature on the otherhand. (redcurve)

The daily returns mainly move in a narrow corridor (with a longbias) and thus deviate from the normal distribution. We can take advantage of this small movement.

The yield curve of our strategy benefits from the small movements of the market around the mean. We have therefore modeled the pay off profile on the market behavior, so that we can achieve an additional return due to the positive kurtosis, respectively the small daily fluctuations around the mean.



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SOURCE OF ALPHA NO. 4

QUANTITATIVE TREND FOLLOWING MODEL

This option combination consists of long calls/puts and short calls/puts. It is structured in such a way that the yield curve moves upwards over a wide price range until shortly before the option expires. In this way, profits are generated after a few days even if prices fall. The only risk of loss with this option combination is a possible strong sell-off of the underlying, immediately after opening the option positions.

Example:



Therefore, our proven trend following, and momentum model is used for trend determination, measuring the primary stock trend and the current stock climate. Difficult market phases are systematically avoided by this quantitative trendfilter. The option strategy is opened exclusively when the stock climate is positive, and an intact up trend is measured.

SOURCE OF ALPHA NO. 5

MEAN REVERSION MODEL AND OPTIMIZATION OF SHORT VOLATILITY RETURNS

Our tactical mean reversion model shows short term lows in a bull market and has several advantages: Position building occurs in a correction of the up trend at more favorable entry prices. Due to the high hit rate of these models, the loss area in the option strategy is reached very rarely and draw down and volatility are reduced. The inverse behavior of the VIX to the stock market allows this strategy to open with higher volatility and thus at better entry prices.

When the primary trend resumes, the options strategy benefits from both an increase in price and a decrease in volatility (VIX).

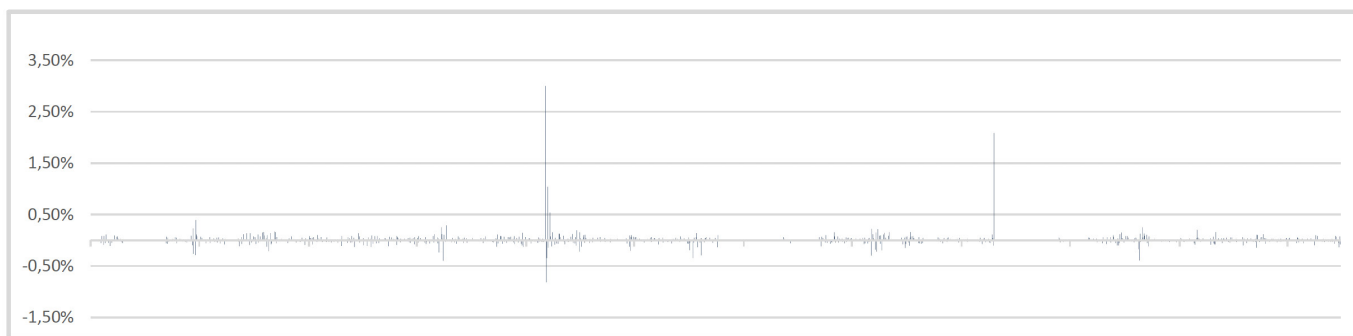


Example: Mean-Reversion entry-points and inverse behaviour of VIX / S&P500

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DAILY SPIKES ANALYSIS



With the Black-Swan hedge the total average volatility is slightly higher, because the positive effect of the hedge on the upside volatility also raises the total volatility and reduces the overall Sharpe-Ratio. The high daily spikes logically appear mostly on the pos-

itive side due to the embedded hedge. The average daily spike is around 0,00688%. The maximum down-spike was 0,81% on one day in the entire history of the portfolio strategy forward-test.

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Jochen Deecke founded DEECKE HOLDING after switching from medicine to the world of finance. For more than 35 years, he has been developing successful investment strategies and financial solutions.



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